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Senator John Cornyn
517 Hart Senate Office Building
Washington, DC 20510

RE: Bankruptcy Venue Reform

Dear Senator:

I commend efforts, either through an amendment to the bankruptcy bill before Congress or through the separate vehicle being introduced by Senator Cornyn, to close a major jurisdictional loophole in the bankruptcy statutes which directly affects every investor, business competitor, creditor, consumer, union, and state Attorney General in this country. While forum shopping and court competition are having a direct, adverse effect on the governance and reorganization of large, public companies, investors are feeling that effect in their returns; employees and unions in the abrogation of collectively bargained contracts and economic security; competitors in the loss of a level playing field; consumers and creditors in the loss of basic rights; and Attorneys General in the loss of power to be heard and to protect the rights of constituents and state public policy.

For the past decade, most bankrupt large public companies have "forum shopped" their cases to the bankruptcy courts in Wilmington, Delaware and New York City. For a time, that was generally thought to be advantageous. But events in Enron and other cases have shown otherwise. The shopping benefited bankruptcy professionals who worked in those cases by enabling them to charge higher fees and by freeing them from some restrictions on conflicts of interest. The shopping also benefited executives of some of those companies by allowing them to hang onto their jobs longer and in some cases even be paid large "retention bonuses."

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But the effect of forum shopping on the companies – and hence on the shareholders and bondholders who invested in them – has been decidedly negative. According to major studies and the empirical research of experts like Professor Lynn LoPucki of UCLA law school, companies reorganized in the Delaware and New York courts in the early and mid-1990s failed at a rate more than double the rate for companies reorganized in other courts. As other courts copied Delaware in an effort to staunch their outflow of cases, the failure rates for those courts' reorganizations skyrocketed to match Delaware's rates. To confirm a plan, the Bankruptcy Code requires that the court find that "confirmation . . . is not likely to be followed by the liquidation, or the need for further financial reorganization of the debtor." But of the 43 largest public companies reorganized in U.S. Bankruptcy Courts from 1997 through 2000 – the most recent period for which failure rates can be calculated – 21 (49%) were back in bankruptcy within five years. Historically, the failure rates for big reorganization in non-competing courts have been below 10%.

Legislative action can address this problem in a common sense, fair, simple and direct way, by requiring bankrupt companies file in their local bankruptcy courts. By local courts, I mean the courts in the cities where the companies have their headquarters or their principal operations. This will free judges from the pressures to compete with other courts for cases, and enable them to return to the crucial function for which they were appointed: to protect shareholders, creditors, employees, suppliers, customers and the companies themselves during the brief but often frantic period between the failure of one corporate regime and its replacement with another. It will also ensure that these judges and courts hear from everyone affected and entitled to be heard – not only those who can afford to travel or appear in 'foreign" courts, especially the public's lawyers, the Attorneys General. It is not a panacea for economic insecurity, and it changes no legal rights or duties or law. But it will cure a major inequity and a loophole utilized primarily to "game" the system. Enactment of this bill, or a similar legislative amendment, will enable us to say: "We had a problem, and now we have fixed it."

Scott Harshbarger, Massachusetts Attorney General, 1991-1999